

SENATE BILL 1195
By Henry

AN ACT to amend Tennessee Code Annotated, Section 8-4-113
and Title 9, Chapter 18, to enact the "Internal Control Act
of 1997".

BE IT ENACTED BY THE GENERAL ASSEMBLY OF THE STATE OF TENNESSEE:

SECTION 1. Tennessee Code Annotated, Title 9, Chapter 18, is amended by deleting
Parts 1 through 4 in their entirety and by substituting instead Sections 2 through 8 of this act.

SECTION 2. This chapter shall be known and may be cited as the "Internal Control Act
of 1997".

SECTION 3. The purpose of this act shall be to require each agency of state
government to establish and maintain an effective system of internal control which provides
reasonable assurance of:

(1) The economy and efficiency of government operations, including the
safeguarding of public assets against loss, use of resources, and the achievement of
agency objectives, purposes and goals;

(2) The preparation, publishing, and reporting of reliable financial information,
including, when applicable, financial statements and operational data;

(3) Compliance with applicable laws, regulations, policies, contracts, and grants.

It shall be the public policy of the state of Tennessee that the chief executive officer of each
agency of state government is responsible for effectively and efficiently managing the agency
and establishing and maintaining an effective system of internal control. An emphasis shall be

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placed on results, outcomes, attainment of goals and performance measures, and improvements. This act shall be liberally construed to carry out this public policy.

SECTION 4. The internal control system of each agency shall consist of five (5) interrelated components which shall be integrated into the management process of the agency. It is the responsibility of top management to ensure that the components have been effectively developed and implemented. To that end top management shall appropriately delegate and oversee the implementation of these requirements. The five (5) internal control system components shall be as follows:

(1) A control environment providing the foundation for all other components of the internal control system. A sound control environment must provide structure and discipline to the internal control system. The sound control environment shall include:

(A) Written evidence of the agency's commitment to the achievement of integrity, ethical values, and competence of agency management and employees;

(B) Express documentation relative to the achievement of:

(i) An effective and efficient management philosophy and operating style;

(ii) Proper assignment of authority and responsibility;

(iii) Proper organization of available resources;

(iv) Proper training and development of employees; and

(v) Proper attention and direction provided by agency management.

(2) Adequate risk assessment designed to identify and analyze relevant risks and to achieve agency objectives. Each agency will be required to document the risk assessment process and the resulting findings, recommendations, and corrective actions taken. Each agency will be required to assess risk from external and internal

sources. The risk assessment shall be performed annually and be completed no later than June 30 of each year. Such risk assessment shall include:

(A) the identification and analysis of risk and the formation of a basis for determining how risks will be managed.

(B) establishment of a set of objectives that integrate all the agency's resources so that the agency can operate in concert.

(C) establishment of mechanisms in place to identify risks associated with changes in economic, technological, industry, regulatory, and operating conditions.

(3) Agency control activities shall include the establishment and execution of written policies and procedures to help ensure the timely, effective, and efficient implementation of the agency's mandates and directives. These control activities shall ensure that the agency's mandates and directives are carried out at all levels of the agency; and in all activities, units and functions. Control activities shall include, but not be limited to approvals, authorizations, reviews of operating performance, security of assets, and segregation of duties.

(4) Each agency shall implement a formal information and communication system which produces timely reports containing operational, financial, and compliance related information that makes it possible to effectively and efficiently operate the agency. The information system shall pertain not only to internally generated data, but also information concerning external events, activities and conditions necessary for informed agency decision-making and external reporting. The information and communication system will incorporate the following:

(A) Pertinent information will be identified, captured, and communicated in a form and time frame that enables employees to carry out their responsibilities;

(B) Effective communication will occur between all levels and employees of the agency and will stress the intent that control responsibilities are to be considered vital to the agency's functions;

(C) All employees will understand their role in the internal control system;

(D) All employees will have a means of communicating significant information to higher levels of agency authority;

(E) Effective communication will also exist with external parties including other agencies, legislators, and regulators.

(5) Monitoring of the entire internal control system must take place to assess the quality of the system's performance over a period of time. Ongoing internal monitoring of management and supervisory activities, and actions of employees taken in performing their duties will occur during the normal course of operations. Effective monitoring shall also include:

(A) The reporting of internal deficiencies to appropriate supervisors and agency heads;

(B) A separate and independent evaluation of the internal control system by top management. The scope and frequency of the independent evaluation will depend primarily upon the assessment of risk and the effectiveness of ongoing monitoring procedures. However, an independent evaluation for the agency as a whole shall be performed by top management and documented at least annually.

SECTION 5. The commissioner of finance and administration, in consultation with the comptroller of the treasury, shall establish guidelines for the evaluation by agencies of their systems of internal control to determine such system's compliance with the requirements of this act. The commissioner, in consultation with comptroller of the treasury, may modify such guidelines from time to time as deemed necessary.

SECTION 6. The supreme court and constitutional officers shall establish procedures to annually assess the adequacy of internal controls for activities within their respective entities, using procedures consistent with the intent of this act.

SECTION 7. This act shall become effective upon becoming law, the public welfare requiring it.

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